**AIC DOTCOM SDN BHD**

**v.**

**MTEX CORPORATION SDN BHD & ORS**

HIGH COURT MALAYA, KUALA LUMPUR
VINCENT NG J
[SUIT NO: D1-24-41-2002]
18 JULY 2003

***COMPANY LAW:*** *Rights of minority - Locus standi - Whether plaintiff had locus standi to initiate action - Whether action brought for the benefit of the company - Parties - Whether plaintiff made attempts to secure other shareholders to sue defendants - Allegation of defendants' wrongdoings amounting to losses and damages suffered - Whether proved - Whether plaintiff's action could be struck out under O. 18 r. 19(1) Rules of the High Court 1980*

***CIVIL PROCEDURE:*** *Locus standi - Action to sue as representatives of company - Failure to plead present action as derivative action in statement of claim - Whether deficient - Whether action brought for benefit of company - Whether plaintiff had locus standi to initiate action - Allegation of defendants' wrongdoing amounting to losses and damages suffered - Whether borne out by any evidence - Whether plaintiff's action could be struck out under O. 18 r. 19(1) Rules of the High Court 1980*

***CIVIL PROCEDURE:*** *Pleadings - Striking out, application for - Rules of the High Court 1980, O. 18 r. 19(1)(b), (d) - Failure to plead derivative action - Whether there was deficiency in statement of claim - Whether there was indication of plaintiff's attempts to secure other shareholders to sue defendants - Whether plaintiff's action could be struck out under O. 18 r. 19(1) Rules of the High Court 1980*

The plaintiff sued the defendants as representatives of MTEX Corporation Sdn Bhd (MTEX) and alleged that in breach of her fiduciary duties, the second defendant had purportedly utilised confidential information to develop and operate the third defendant, had infringed the plaintiff's copyright of MTEX software and had diverted businesses away from MTEX, resulting in loss and damages suffered by MTEX. The defendants contended, primarily that the plaintiff lacked *locus standi* to bring this action and sought to strike out the plaintiff's claim against them, premised on O. 18 r.19 of the Rules of the High Court 1980, which was subsequently allowed by the senior assistant registrar. The plaintiff appealed against that decision.

**Held:**

**[1]** The plaintiff's statement of claim was deficient for failure to plead that the present action was a derivative action; brought for the benefit of the plaintiff, other minority shareholders and MTEX because MTEX themselves were unable to sue the second and third defendants for their alleged wrongdoings. The plaintiff's own statement of the current shareholding in MTEX and its allegation that the second defendant was in control of MTEX and therefore in a position to block any intended action against herself and the third defendant was not borne out by any evidence. Furthermore, there was nothing in the pleadings to indicate that the plaintiff had made any kind of attempt to get the other shareholders or MTEX to sue the second and third defendants. (p 156 a-c)

*[Appeal dismissed.]*

**Case(s) referred to:**

*Abdul Rahim Aki v. Krubong Industrial Park (Melaka) Sdn Bhd [1995] 4 CLJ 551 CA* ***(refd)***

*Australian Coal & Shale Employees Federation v. Smith [1937] 38 SR (NSW) 48* ***(refd)***

*Biala Pty Ltd & Anor v. Mallina Holdings Ltd & Ors 11 ACSR 785* ***(dist)***

*Burland v. Earle [1902] AC 83* ***(refd)***

*Christianos & Ors v. Aloridge Pty Ltd & Anor 18 ACSR 272* ***(refd)***

*Edwards v. Halliwell [1950] 2 All ER 1064* ***(refd)***

*Eromanga Hydrocarbon NL v. Australis Mining NL & Ors 14 ACLR 486* ***(refd)***

*Ferguson v. Wallbridge [1935] 3 DLR 66* ***(refd)***

*Foss v. Harbottle [1843] 67 ER 189* ***(refd)***

*Gilbert Engineering Co Inc v. Zainuddin Ahmad & Ors [2001] 7 CLJ 489 HC* ***(refd)***

*MacDougall v. Gardiner [1875] 1 Ch D 13* ***(refd)***

*Menier v. Hoper's Telegraph Works [1874] LR 9 Ch 350* ***(refd)***

*Prudential Assurance Co Ltd v. Newman Industries Ltd (No 2) [1982] Ch 204* ***(refd)***

*Tan Guan Eng & Anor v. Ng Kweng Hee & Ors [1991] 3 CLJ 1881; [1991] 4 CLJ (Rep) 74 HC* ***(refd)***

**Legislation referred to:**

Rules of the High Court 1980, O. 18 r. 19(1)(a), (b)

*For the appellant/plaintiff - Gideon Tan (HS Wong); M/s Gideon Tan Razali Zaini*
*For the respondents/2nd & 3rd defendants - Teh Meng Teck (Winnie Chan); M/s Cheah Teh & Su*

*Reported by Suhainah Wahiduddin*

## JUDGMENT

**Vincent Ng J:**

**Preamble**

On 9 March 2002, the learned senior assistant registrar allowed the second and third defendants' application to strike out the plaintiff's claim against them.

The second and third defendants' application to strike out the plaintiff's claim, premised on O. 18 r. 19(1)(a) and/or alternatively O. 18 r. 19(1)(b) and/or (d) of the Rules of the High Court 1980 (RHC) and/or the inherent jurisdiction of the court, was focused on the question of the plaintiff's *locus standi* to bring this action.

Enclosure 50 is the plaintiff's appeal against that decision.

**The Law**

I remind myself of the trite principles of striking out under O. 18 r. 19(1)(a) of the RHC I had occasion to set out in *Gilbert Engineering Co Inc v. Zainuddin bin Ahmad & 5 Ors* [2001] 7 CLJ 489 at p. 491:

> ...
>
> (a) no affidavit/evidence shall be admissible; and
>
> (b) the court must consider only the pleadings for the purpose of determining whether the statement of claim disclosed no reasonable cause of action – the test to be applied is whether on the face of the pleading the Court could hold that the cause of action or defence is obviously unsustainable.

In *Foss v. Harbottle* [1843] 67 ER 189 *(Foss v. Harbottle)*, the English Court propounded the proposition that in company law, if a wrong had been done to a company, then it was the company which was the proper plaintiff in an action brought to redress the injury. An individual shareholder or even a group of shareholders forming a minority did not have the *locus standi* to bring an action to remedy a wrong done to a company. (See *Prudential Assurance Co Ltd v. Newman Industries Ltd (No 2)* [1982] Ch 204 and *Edwards v. Halliwell* [1950] 2 All ER 1064.)

In *Abdul Rahim bin Aki v. Krubong Industrial Park (Melaka) Sdn Bhd* [1995] 4 CLJ 551, Gopal Sri Ram JCA, delivering the judgment for the Court of Appeal, expressed the following views on the exception to the *Foss v. Harbottle* principle:

> It is the derivative action; ... It is based upon the premise that the company which has been wronged is unable to sue because the wrongdoers are themselves in control of the decision-making organs and will not, for that reason, permit an action to be brought in its name. In these circumstances, a minority shareholder may bring an action on behalf of himself and all the other shareholders of the company, other than the defendants. The wrongdoers must be cited as defendants. So must the company. The title to the action must reflect that the suit is being brought in a representative capacity. The statement of claim or other pleading filed in support of the originating process must disclose that it is a derivative action and recite the facts that make it so. Further, there must be an express statement in the pleading that the action is being brought for the benefit of the company named as a defendant. An action that does not meet these requirements is liable to be struck out as being frivolous and vexatious.
>
> The juridical basis upon which the court entertains such an action is that the majority who have either *de facto* or *de jure* control of the company have, by commission or omission, committed what is described as 'a fraud upon the minority' ...

The decision of the English Court of Appeal in *Wallerstein v. Moir (No 2)* [1975] QB 373, is regarded as the high-level watermark of the law and procedure governing derivative actions in the sphere of company law. Lord Denning ... said:

> It is a fundamental principle of our law that a company is a legal person, with its own corporate identity, separate and distinct from the directors or shareholders, and with its own property rights and interests to which alone it is entitled. If it is defrauded by a wrongdoer, the company itself is the one person to sue for the damage. Such is the rule in *Foss v. Harbottle* [1843] 2 Hare 461. The rule is easy enough to apply when the company is defrauded by outsiders. The company itself is the only person who can sue. Likewise, when it is defrauded by insiders of a minor kind, once again the company is the only person who can sue. But suppose it is defrauded by insiders who control its affairs – by directors who hold a majority of the shares – who then can sue for damages? Those directors are themselves the wrongdoers. If a board meeting is held, they will not authorise the proceedings to be taken by the company against themselves. If a general meeting is called, they will vote down any suggestion that the company should sue them themselves. Yet the company is the one person who is damnified. It is the one person who should sue. In one way or another some means must be found for the company to sue. Otherwise the law would fail in its purpose. Injustice would be done without redress. In *Foss v. Harbottle* 2 Hare 461 at pp. 491-492, Sir James Wigram V-C saw the problem and suggested a solution. He thought that the company could sue 'in the name of someone whom the law has appointed to be its representative'. A suit could be brought:

> by individual corporations in their private characters, and asking in such character the protection of those rights to which in their corporate character they were entitled, ...

This suggestion found its fulfilment in the *Merryweather* case (The reference here is to *Atwool v. Merryweather*) which came before Sir William Page Wood V-C on two occasions: see [1864] 2 Hem & M 254 (sub nom *East Pant Du United Lead Mining Co Ltd v. Merryweather*) and LR 5 Eq 464n. It was accepted there that the minority shareholders might file a bill asking leave to use the name of the company: see 2 Hem & M 254 at p 259; LR 5 Eq 464n at pp. 467-468n. If they showed reasonable ground for charging the directors with fraud, the court would appoint the minority shareholders as representatives of the company to bring proceedings in the name of the company against the wrongdoing directors. By that means the company would sue in its own name for the wrong done to it. That would be, however, a circuitous course, as Lord Hatherley LC said himself, at any rate in cases where the fraud itself could be proved on the initial application.

To avoid the circuity, Lord Hatherley LC held that the minority shareholders themselves could bring an action in their own names (but in truth on behalf of the company) against the wrongdoing directors for the damage done by them to the company, provided always that it was impossible to get the company itself to sue them. He ordered the fraudulent directors in that case to repay the sums to the company, be it noted, with interest: see LR 5 Eq 464n at p. 469n. His decision was emphatically approved by this court in *Menier v. Hooper's Telegraph* [1874] 9 Ch App 350 and *Mason v. Harris* [1879] 11 Ch D 97. The form of the action is always 'AB (a minority shareholder) on behalf of himself and all other shareholders of the company' against the wrongdoing directors and the company. That form of action was said by Lord Davey to be a 'mere matter of procedure in order to give a remedy for a wrong which otherwise would escape redress': see *Burland v. Earle* [1902] AC 83 at p. 93. Stripped of mere procedure, the principle is that, where the wrongdoers themselves control the company, an action can be brought on behalf of the company by the minority shareholders on the footing that they are its representatives to obtain redress on its behalf.

I am glad to find this principle well stated by Prof Gower in *Modern Company Law* (3rd Edn, 1969) at p. 587, in words which I would gratefully adopt:

> Where such an action is allowed, the member is not really suing on his own behalf nor on behalf of the members generally, but on behalf of the company itself. Although ... he will have to frame his action as a representative one on behalf of himself and all the members other than the wrongdoers, this gives a misleading impression of what really

> occurs. The plaintiff shareholder is not acting as a representative of the other shareholders, but as a representative of the company. ... In the United States ... this type of action has been given the distinctive name of a 'derivative action', recognising that its true nature is that the individual member sues on behalf of the company to enforce rights derived from it. ...
>
> We emphasise that it is not permissible for a plaintiff in a derivative action to sue in his own name, without indicating that he is bringing the action in a representative capacity and for the benefit of the company of which he is a shareholder. (emphasis added).

(See *Tan Guan Eng & Anor v. Ng Kweng Hee & Ors* [1991] 3 CLJ 1881; [1991] 4 CLJ (Rep) 74, *MacDougall v. Gardiner* [1875] 1 Ch D 13 at 21, *Burland v. Earle* [1902] AC 83 at 93, *Menier v. Hoper's Telegraph Works* [1874] LR 9 Ch 350 and *Australian Coal & Shale Employees Federation v. Smith* [1937] 38 SR (NSW) 48 at 54.)

Guided by these principles, I scrutinised the plaintiff's statement of claim with a fine-tooth comb.

**Pleadings**

The plaintiff had entitled the present civil action as a derivative action, whereby they were suing the defendants as representatives of MTEX Corporation Sdn Bhd (MTEX). *Vide* para. 8 of the plaintiff's statement of claim, the current shareholding of MTEX is as follows:

(i) Plaintiff – 35%;

(ii) World Computer Technology Sdn Bhd – 30%; and

(iii) Red Stream Multimedia Sdn Bhd – 35%.

The plaintiff identified the second defendant as one of the key MTEX founder persons; holding the post of director from 29 October 1999 till 31 May 2001. Aside from being the shareholder and executive director of the third defendant, the second defendant also held interests in World Computer Technology Sdn Bhd.

The plaintiff alleged that in breach of her fiduciary duties, the second defendant purportedly utilised confidential information to develop and operate the third defendant as a competing business. The second defendant allegedly infringed the plaintiff's copyright of MTEX software. Further, the plaintiff accused the second defendant of diverting businesses away from MTEX.

The closing paragraphs of the plaintiff's statement of claim reads:

> 17. By reasons of the matters aforesaid, **MTEX has suffered losses and damages.**
>
> 18. The second and third defendants ... whereby **MTEX will suffer further loss and damages.**
>
> Wherefore the plaintiff in its representative capacity claims against the second and third defendants ...
>
> (ii) that the second and third defendants, their servants or agents, be restrained from using, copying or utilising **the MTEX software ...** (emphasis added)

**The Appeal**

The plaintiff's statement of claim flies in the face of the *Foss v. Harbottle* principle; which is why they sought to rely on the fifth exception to it as set out in *Biala Pty Ltd & Anor v. Mallina Holdings Ltd and Ors* 11 ACSR 785 *(Biala)*:

> The Courts should not shrink from determining whether the justice of the case should allow a shareholder to proceed with a derivative action ... Equity is concerned with substance and not form and it seems to me to be *contrary to principle to require wronged minority shareholders to bring themselves within the boundaries of well-recognised exceptions and to deny jurisdiction even where an unjust or unconscionable result may otherwise ensue.*
>
> The circumstances of modern commercial life are very different to those which existed when *Foss v. Harbottle* was decided. ...These developments and the complexities and sophistication of modern shareholding make it often very difficult to bring derivative claims within the established exceptions. ... *I consider it to be desirable to allow a minority shareholder to bring a derivative claim where the justice of the case clearly demands that such a claim be brought, irrespective of whether the claim falls within the confines of established exceptions.* (emphasis added).

(See *Eromanga Hydrocarbon NL v. Australis Mining NL & Ors* 14 ACLR 486 and *Christianos & Ors v. Aloridge Pty Ltd & Anor* 18 ACSR 272.)

The plaintiff's reliance on the Australian case is misconceived. The rationale of the court in *Biala*, in allowing the derivative action to continue under the 'justice of the case' exception is because the court recognised that factually it was the most unusual case they had encountered; where 'fraud on the minority has been established at the date of the writ, but where, thereafter, the majority have disposed of most of their shares to defeat the allegation that at the time of trial they were in control of the company'.

The facts of the present action are straightforward. The plaintiff's statement of claim is deficient for failure to plead that the present action is a derivative action; brought for the benefit of the plaintiff, other minority shareholders and MTEX because MTEX themselves were unable to sue the second and third defendants for their alleged wrong doings.

In light of the plaintiff's own statement of the current shareholding in MTEX, their allegation that the second defendant was in control of MTEX and therefore in a position to block any intended action against herself and the third defendant is not borne out by any evidence. Furthermore, there is nothing in the pleadings to indicate that the plaintiff had made any kind of attempt to get the other shareholders or MTEX to sue the second and third defendants.

I am *ad idem* with Lord Blanesburgh, speaking for the Privy Council in *Ferguson v. Wallbridge* [1935] 3 DLR 66 wherein he held:

> ... even in a case of a going company *a minority shareholder is not entitled to proceed in a representative action if he is unable to show when challenged that he has exhausted every effort to secure the joinder of the company as plaintiff and has failed.* (emphasis added).

**Conclusion**

For the reasons stated above, the plaintiff's appeal is doomed to fail. Accordingly I dismiss encl. 50 with costs to the defendants.